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DE RUEHCV #2450/01 2291836  
ZNR UUUUU ZZH  
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FM AMEMBASSY CARACAS  
TO RUEHC/SECSTATE WASHDC 5884  
INFO RUEHBO/AMEMBASSY BOGOTA 6913  
RUEHLP/AMEMBASSY LA PAZ AUG LIMA 0525  
RUEHZP/AMEMBASSY PANAMA 1093  
RUEHQT/AMEMBASSY QUITO 2365  
RUEHSG/AMEMBASSY SANTIAGO 3719  
RUEHGL/AMCONSUL GUAYAQUIL 0604  
RHEHNSC/NSC WASHDC  
RUCPDOG/DEPT OF COMMERCE  
RHEBAAA/DEPT OF ENERGY  
RUEATRS/DEPT OF TREASURY

UNCLAS CARACAS 002450

SIPDIS

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DEPARTMENT FOR L/CID/JNICOL AND EB/IFD/OIA/NHATCHER

E.O. 12958: N/A  
TAGS: [EINV](#) [KIDE](#) [OPIC](#) [PGOV](#)  
SUBJECT: 2006 SECTION 527 REPORT ON INVESTMENT DISPUTES IN  
VENEZUELA

REF: STATE 60294

(1.) The following is the 2006 Section 527 report on investment disputes in Venezuela. Two claims from the 2005 report have been resolved. Claimant identities are listed separately per reftel instructions.

(2.) (SBU) RESOLVED CLAIM:

a. Claimant A (Resolved)

b. 2003

c. Case History: In 2001, Claimant A, an international consortium with a 55 percent US share, entered into a ten-year contract to operate a key petroleum export terminal for Venezuela's state-owned oil company, Petroleos de Venezuela (PDVSA). On December 6, 2002, as a result of Venezuela's petroleum strike, Claimant A declared its inability to implement the contract due to force majeure. Claimant A's employees continued to perform the necessary maintenance so that the terminal could be brought back into operation quickly once the conditions that necessitated the terminal to be shutdown were resolved. The terminal, however, was seized by the BRV on December 15 and Claimant A's employees were forbidden access. Claimant A stated the case has been successfully resolved through consensus involving both parties. No significant details on the arrangement reached are available as the claimant signed a confidentiality agreement with the state-owned oil company

SIPDIS  
Petroleos de Venezuela (PDVSA).

a. Claimant B:

b. 2002

c. Case History: In 1993, Claimant B entered into a long-term relationship with Venezuela's state-owned oil company Petroleos de Venezuela (PDVSA) and with PDVSA-affiliate CITGO, in which: (1) Claimant B agreed to invest over \$1.1 billion to upgrade its refinery to process Venezuelan extra-heavy crude, (2) CITGO agreed to contribute to the upgrading and purchase the bulk of the refined

products, and (3) PDVSA committed to supply 230,000 barrels/day for 25 years. Two contracts, one signed under Venezuelan law and one signed under US law, established this relationship. Claimant B asserts that between April 1998 and September 2000, PDVSA, citing BRV commitment to OPEC quota cuts, wrongfully declared force majeure and reduced its deliveries by as much as 100,000 barrels/day. This force majeure was lifted in October 2000, but in January 2002 PDVSA once again informed Claimant B that deliveries would be cut because of OPEC quota cuts. Claimant B attempted to resolve the dispute but ultimately filed suit against PDVSA on February 1, 2002 before the United States District Court for the Southern District of New York, seeking damages and specific compliance. On May 31, 2002, PDVSA filed a motion to dismiss Claimant B's suit arguing protection under the "Act of State doctrine."

The claimant's attorney reported that the United States District Court for the Southern District of New York urged the parties to reach an agreement on the case. The parties dismissed the suit from the court with Venezuela agreeing to negotiate the sale of its share in the refinery. On August 15 2006, Venezuela's Minister of Energy and Mines announced an agreement for the Claimant to buy Venezuela's 41.25 percent ownership participation in the disputed investment. Previously, the Venezuelan party stated it would not object to the sale to the Claimant if the Claimant matched best offer received from third parties. According to the Claimant, the claimant will purchase the Venezuelan party's share for approximately USD 2.1 billion. The main cause of this dispute, an oil supply agreement which remained valid for 17 years, was terminated and replaced with a 5 year agreement with no legal assurance of renewal. On August 16, 2006, the Claimant confirmed the agreement.

(3.) (SBU) UNRESOLVED CLAIMS:

a. Claimant C:

b. 2003

c. Case History: Since 1982, Claimant C, an international consortium of investors with a majority US share, has invested approximately \$60 million in developing a diamond concession in Venezuela's Bolivar state. After extensive exploration and evaluation of the asset, Claimant C planned to begin mine development in 2003-2004. However, in September 2003, the Venezuelan Ministry of Energy and Mines withdrew part of Claimant C's concession, alleging non-payment of taxes and failure to comply with other obligations. Claimant C disputes these allegations. The Embassy and U.S. congressional representatives have raised the case with the senior BRV offices. Thus far, there has been no return of the concession and four additional concessions previously granted to this claimant were withdrawn in the first quarter of 2005. Claimant C sought a protective measure before Venezuela's Supreme Court for the withdrawal of the concessions. The request has been acknowledged and accepted by the tribunal but there have been no significant developments. Claimant C reported that it is confident that if a decision is reached objectively, the company will receive an affirmative finding. The mining reform bill currently under discussion in the National Assembly, which calls for the formation of mixed companies in the mining sector, is viewed as a positive development by Claimant C.

a. Claimant D:

b. 1994

c. Case History: Claimant D, an airline, accrued \$23 million in foreign exchange losses due to actions taken by the Central Bank of Venezuela (BCV) before and after a devaluation of the currency in 1995. BCV imposed currency controls in 1994, which compelled Claimant D to purchase all

dollars through the Central Bank. The official exchange rate at that time was 290 bolivars to one dollar. Additionally, a 1994 presidential decree obligated the Claimant D to sell all airline tickets in Venezuela in bolivars, at the official rate. In early 1995, BCV stopped exchanging bolivars for dollars for several months immediately prior to a significant devaluation of the currency from 290 to 470 bolivars/\$1. The claimant maintains that the devaluation resulted in a \$23 million loss to the amount held in escrow. The claimant brought suit against the BRV in July 1996, but the Supreme Court of Venezuela dismissed the suit in May 1998. Claimant D resubmitted the case in 1999, and a chamber of the Court made a decision against it in March 2003 and additionally assessed Claimant D for court costs and all legal fees. Claimant D appealed this ruling in 2004.

Claimant D reported it continues to appeal the excessive court costs and legal fees associated with the ruling by the Supreme Court, but does not contest the Court's ruling. No major developments can be reported.

a. Claimant E:

b. 2001

1C. Case History: In 1996, Claimant E and Venezuela's state-owned oil company, Petroleos de Venezuela (PDVSA), entered into a joint venture agreement. In 2002, after several disagreements between the two parties, Claimant E and PDVSA started negotiations to dissolve the joint venture and to transfer Claimant E's shares to PDVSA. This situation was exacerbated by the December 2002-February 2003 general strike, during which the joint venture company ceased to provide services to PDVSA. In September 2003, Claimant E

filed a claim under OPIC political risk insurance, stating its investment had been expropriated. On February 24, 2004, OPIC made a final determination in support of this claim and made a final payment to the insured on May 12, 2004. The claimant's lawyer reported that OPIC has not pursued the claim in Venezuelan court.

a. Claimants F1, F2, F3:

b. 2004

c. Case History: In October 2004, the BRV announced a decision to increase royalty payments by the four extra-heavy crude oil projects in Venezuela. Effective immediately, royalties were raised from 1 percent to 16.67 percent. Claimants F1, F2, and F3 have stakes in three of the four projects affected by this decision. These projects were negotiated in the mid-1990's, and as an incentive for the investment and risk of the projects, the BRV agreed to take a 1 percent royalty until the individual projects had recouped some multiple of their investment or until nine years had passed, whichever came first. The decision by the BRV appears to violate this agreement. Of the three claimants, only Claimant F1 continues to reserve its right to arbitration. Current moves by the Venezuelan government to increase its participation and gain a controlling position in the extra-heavy crude ventures complicate any arbitration filings on the royalty increase.

a. Claimants G1, G2, G3, G4, G5:

b. 2005

1C. Case History: Since late 2004, the BRV has taken a number of steps to force the oil companies holding Operating Service Agreement (OSA) contracts negotiated under a previous government in the mid-1990's to convert their assets into minority stakes in joint ventures with Venezuela's state oil company PDVSA under the 2001 Hydrocarbons law. These steps have included limiting capital expenditure budgets and refusal to approve drilling permits. The national tax

authority SENIAT has also claimed retroactively that OSA companies are production companies rather than service companies and were subject to 50 percent tax rates for 2002-2004 and 66.67 percent for 2001 rather than the 34 percent business tax rate that had been agreed. Claimants G1, G3, G4, and G5 signed transitory agreements to migrate from OSAs to joint venture companies. However, the claimants G1, G4, and G5 have not yet signed their mixed company agreements setting up the new joint ventures and currently operate in a state of legal limbo. Claimant G2 sold its stake in the OSA to avoid the consequences of the forced migration. G3 has signed their joint venture agreement and is in the process of migrating its assets to the new joint venture.

#### 14. (SBU) CLAIMANT ID LIST

Claimant A: Sociedad Williams Enbridge Y Compania (SWEC). The SWEC consortium includes the Tulsa-based Williams Company (45 percent share); Enbridge Inc., a Canadian firm with a 45 percent share; and the U.S.-based Northville Industries Inc. with a 10 percent share.

Claimant B: Lyondell Chemical Company

Claimant C: Guaniamo Mining Company

Claimant D: American Airlines

Claimant E: Science Applications International Corporation (SAIC) and joint venture company INTESA

Claimant F1: ExxonMobil

Claimant F2: ConocoPhillips

Claimant F3: ChevronTexaco

Claimant G1: Harvest Resources

Claimant G2: ExxonMobil

Claimant G3: ChevronTexaco

Claimant G4: Andarko Petroleum

Claimant G5: Williams

WHITAKER